

FINANCIAL STATEMENTS AND REPORT OF
INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS
SOUTHWEST MEDICAL CENTER
DECEMBER 31, 2011 AND 2010

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SOUTHWEST MEDICAL CENTER
MANAGEMENT'S DISCUSSION AND ANALYSIS
Years ended December 31, 2011 and 2010

Our discussion and analysis of the financial performance of Southwest Medical Center provides a narrative overview of the Medical Center's financial activities for the years ended December 31, 2011 and 2010. Please read it in conjunction with the accompanying basic financial statements.

Financial highlights

The Medical Center's net assets increased during each of the past two years with a \$721,128 or 2.2 percent increase in 2011 and a \$391,548 or 1.2 percent increase in 2010.

The Medical Center reported a \$253,462 or 59.3 percent increase in operating income for 2011 and a \$115,195 or 36.8 percent increase in operating income for 2010.

The net assets of Southwest Medical Center Foundation (the Foundation), a component unit of the Medical Center, increased by \$717,887 or 14.3 percent in 2011 and increased by \$448,251 or 9.8 percent in 2010.

Using these financial statements

The Medical Center's financial statements consist of three statements - a Balance Sheet; a Statement of Revenues, Expenses, and Changes in Net Assets; and a Statement of Cash Flows. These financial statements and related notes provide information about the activities of the Medical Center, including resources held by or for the benefit of the Medical Center, and resources restricted for specific purposes by contributors, grantors, and indenture agreements.

One of the most important questions asked about the Medical Center's finances is, "Is the Medical Center, as a whole, better or worse off as a result of the year's activities?" The Balance Sheet and the Statement of Revenues, Expenses, and Changes in Net Assets report information about the Medical Center's resources and its activities in a way that helps answer this question. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. For purposes of these two statements, revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the Medical Center's net assets and changes in them. The Medical Center's net assets - the difference between assets and liabilities - may be thought of as one way to measure its financial health, or financial position. Over time, increases or decreases in the Medical Center's net assets are one indicator of whether its financial health is improving or deteriorating. Consideration must also be given to other nonfinancial indicators, such as changes in the Medical Center's patient base and measures of the quality of service it provides to the community, as well as local economic factors, to assess the overall health of the Medical Center.

The final required statement is the Statement of Cash Flows. The statement reports cash receipts, cash payments, and net changes in cash resulting from operations, investing, and financing activities. It provides answers to such questions as "Where did cash come from?", "What was cash used for?", and "What was the change in cash balance during the reporting period?"

SOUTHWEST MEDICAL CENTER
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED
Years ended December 31, 2011 and 2010

Assets, liabilities, and net assets

The Medical Center's balance sheets as of the end of each of the last three years are summarized as follows:

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Assets			
Current assets	\$11,843,168	\$10,844,571	\$ 9,702,064
Assets limited as to use	16,407,132	30,966,760	18,755,485
Capital assets, net	27,080,743	11,868,063	10,966,655
Other assets	<u>324,106</u>	<u>342,415</u>	<u>24,430</u>
Total assets	<u>\$55,655,149</u>	<u>\$54,021,809</u>	<u>\$39,448,634</u>
Liabilities			
Long-term obligations	\$17,085,941	\$17,281,698	\$ 3,880,595
Current liabilities	<u>4,713,195</u>	<u>3,605,226</u>	<u>2,824,702</u>
Total liabilities	<u>\$21,799,136</u>	<u>\$20,886,924</u>	<u>\$ 6,705,297</u>
Net assets	<u>\$33,856,013</u>	<u>\$33,134,885</u>	<u>\$32,743,337</u>

Cash and cash equivalents in the current asset category increased by \$288,388 during 2011 and increased by \$189,967 during 2010.

Most of the Medical Center's invested cash is set aside by the Board of Trustees for replacement of capital assets or for purchase of additional capital assets. Although, at the discretion of the Board, they may subsequently be used for other purposes, these assets are reported as internally designated assets limited as to use on the balance sheet. This category of assets decreased by \$3,402,045 during 2011 and decreased by \$2,986,342 during 2010. Net transfers were made from operating cash to this category of assets that totaled \$1,800,000 in 2011 and \$90,000 in 2010. Internally designated assets decreased in 2011 and 2010 due to construction expenditures, capital equipment purchases, funding of the debt service reserve fund for the 2010A bonds, and current refunding of the 2001A bonds.

In aggregate, the Medical Center's unrestricted cash and invested cash total was \$12,934,744 and \$16,048,401 as of December 31, 2011 and 2010, respectively. These represent 127 days and 154 days, respectively, of average cash expenses during each of the years then ended. These figures rank near the top quartile of values for other hospitals similar to the Medical Center.

The Medical Center's net patient accounts receivable were 49 percent of current assets as of December 31, 2011, 55 percent as of December 31, 2010, and 52 percent as of December 31, 2009. In relation to net patient service revenue, net patient accounts receivable decreased 1.7 percent during 2011, increased 17.4 percent during 2010, and decreased 13.2 percent during 2009. The average number of days of net patient revenue represented by them was 54 days, 54 days, and 46 days as of December 31, 2011, 2010, and 2009, respectively. The slight decrease in patient accounts receivable that occurred in 2011 was primarily due to improved collections as a result of filled positions in the department. The increase in patient accounts receivable that occurred in 2010 was primarily due to the increase in patient revenues along with unfilled positions in the accounts receivable departments.

SOUTHWEST MEDICAL CENTER
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED

Years ended December 31, 2011 and 2010

At the end of 2011, the Medical Center has \$27,080,743 invested in capital assets, net of accumulated depreciation. The total value of new equipment placed in service totaled \$2,133,029 and \$1,198,454 during 2011 and 2010, respectively. During 2011, the construction project underway added \$11,077,981 for hospital facility additions and renovations and \$3,693,004 for a new medical office building to construction in progress.

During 2010, management of the Medical Center determined that expansion and renovation of its patient service area was necessary to meet the current and future health care delivery demands. Management also decided to construct a medical office building for physician clinics that will be located adjacent to and connected with the Medical Center. This endeavor is being mostly financed by proceeds from the bonds issued during May 2010 in the amount of \$17,670,000. The medical office building is expected to cost \$4,600,000 and will be paid for with available funds of the Medical Center. No new long-term obligations were incurred during 2011. The total for hospital facility additions and renovations included in construction in progress was \$12,892,475 and \$1,814,494 as of December 31, 2011 and 2010, respectively. Medical office building costs included in construction in progress were \$4,017,088 and \$324,084 as of December 31, 2011 and 2010, respectively.

The Medical Center's net assets increased during each of the past three years: \$721,128 or 2.2 percent during 2011, \$391,548 or 1.2 percent during 2010, and \$544,731 or 1.7 percent during 2009. The percentage of total assets financed with net assets, or equity, was 60.8 percent, 61.3 percent, and 83.0 percent as of December 31, 2011, 2010, and 2009, respectively.

The Foundation's balance sheets as of the end of its last three fiscal years ended June 30 are summarized as follows:

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Assets			
Current assets	\$5,216,291	\$4,496,386	\$3,986,156
Capital assets, net	466,135	470,568	448,313
Other investments	<u>65,902</u>	<u>63,487</u>	<u>147,721</u>
Total assets	<u>\$5,748,328</u>	<u>\$5,030,441</u>	<u>\$4,582,190</u>
Liabilities			
Current liabilities	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Net assets	<u>\$5,748,328</u>	<u>\$5,030,441</u>	<u>\$4,582,190</u>

The Foundation's current assets consist primarily of investments in marketable securities. Its net assets increased \$717,887 or 14.3 percent during fiscal year 2011 and increased \$448,251 or 9.8 percent during fiscal year 2010. The increases in net assets were primarily due to more favorable investment market conditions in 2011 and 2010.

SOUTHWEST MEDICAL CENTER
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED
Years ended December 31, 2011 and 2010

Operating results and changes in net assets

The Medical Center's operating results and changes in net assets for each of the last three years are summarized as follows:

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Operating revenues	\$39,801,005	\$40,591,444	\$40,277,551
Operating expenses	<u>39,119,945</u>	<u>40,163,846</u>	<u>39,965,148</u>
Operating income	681,060	427,598	312,403
Interest expense	(202,544)	(269,241)	(216,289)
Nonoperating revenues	(12,388)	153,191	378,617
Capital grants and contributions	<u>255,000</u>	<u>80,000</u>	<u>70,000</u>
Increase in net assets	<u>\$ 721,128</u>	<u>\$ 391,548</u>	<u>\$ 544,731</u>

The first, and most significant, component of the overall change in the Medical Center's net assets is its operating income - generally, the difference between net patient service revenue and the expenses incurred to perform those services. Operating income increased \$253,462 during 2011 and increased \$115,195 during 2010.

Gross and net patient service revenue for the past three years is analyzed as follows:

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Inpatient services	\$32,104,483	\$31,181,315	\$35,882,415
Outpatient services	56,741,539	55,610,943	50,086,631
Physician services	<u>5,612,894</u>	<u>5,609,431</u>	<u>4,111,117</u>
Gross patient service revenue	94,458,916	92,401,689	90,080,163
Contractual adjustments	(48,350,024)	(46,248,010)	(44,016,278)
Provision for bad debts	(4,517,591)	(4,361,559)	(3,998,166)
Charity care	<u>(2,463,196)</u>	<u>(1,830,968)</u>	<u>(2,464,675)</u>
Net patient service revenue	<u>\$39,128,105</u>	<u>\$39,961,152</u>	<u>\$39,601,044</u>

The Medical Center raised its rates for hospital services by 5 percent on January 8, 2010, August 19, 2010, and January 19, 2011. The actual increase in gross patient service revenue was less than expected because of changes in patient utilization.

Total inpatient days decreased by 7.1 percent and total outpatient registrations increased by 11.7 percent during 2011. Total inpatient days decreased by 23.1 percent and total outpatient registrations decreased by 1.9 percent during 2010. Decreased outpatient registrations in 2010 are the result of closing the orthopedic and urology clinics in July 2010, reducing services in the psychiatric outpatient clinic in October 2010, and decreased volumes in emergency room and surgical day care.

SOUTHWEST MEDICAL CENTER
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED
Years ended December 31, 2011 and 2010

In July and August of 2011, the Family Medicine, Orthopedic and ENT clinics opened with employed physicians. In September 2011, the independent surgeons' practice that the Medical Center contracted with closed. A part-time surgeon from that practice was contracted with in October 2011. The Medical Center will also use locum tenens surgeons while searching for permanent replacements for surgeons on the medical staff. At the end of 2011, the Medical Center was in the process of completing negotiations for an employed general surgeon.

In 2010, inpatient surgeries decreased by 16.7 percent and outpatient surgeries decreased by 16.3 percent. These volume fluctuations mirror changes in physician staffing and the continuing trend of increasing outpatient vs. inpatient procedures. In 2010, a family practice physician unexpectedly passed away in July. Also in 2010, the following changes occurred in the employed physician staff: hired two family practice physicians; hired one OB/GYN physician; hired one internal medicine physician, and did not renew the employment contract for one orthopedic and one urologist physician.

The Medical Center has agreements with various third-party payors that provide for payments to the Medical Center at amounts different from its established charge rates. These differences are referred to as contractual adjustments. When expressed as a percentage of gross patient service revenue, the Medical Center's contractual adjustments are comparable to median values for similar hospitals.

The Medical Center provides care free of charge or at amounts less than its established rates to patients who meet certain criteria under its charity care policy. Charity care write-offs increased 34.5 percent in 2011. Charity care write-offs decreased 25.7 percent in 2010. The changes in 2011 and 2010 did not occur as a result of policy or criteria changes. The changes are consistent with health care trends experienced during periods of changing economic conditions. There is also a continuing trend in the health care industry to identify and report the value of charity care provided to patients.

Together, the provision for bad debts and charity care write-offs represented 7.4 percent, 6.7 percent, and 7.2 percent of gross patient service revenue during 2011, 2010, and 2009, respectively, a relatively stable trend.

Employee salaries and wages increased by \$41,793 or 0.2 percent during 2011 and decreased by \$129,377 or 0.8 percent during 2010. These changes are functions of changes in numbers of employees and in pay rates. Average pay rates increased by 2.9 percent and 7.0 percent during 2011 and 2010, respectively. Total full-time equivalent employees decreased by 9 or 2.6 percent during 2011 after decreasing by 27 or 7.3 percent during 2010. The significant decrease in numbers of employees during these two years is primarily due to a reduction in the nonclinical work force and discontinuing psychiatric inpatient services which occurred in August 2010 and October 2010, respectively.

The cost of employee benefits was 26.0 percent of salaries and wages during 2011 as compared to 27.7 percent of salaries and wages during 2010. Employee benefit expenses decreased \$280,479 during 2011 and increased \$339,092 during 2010. The primary causes of the changes are decreased health insurance claims and decreased recruitment expense during 2011 and increased contributions to the Kansas Public Employees Retirement System during 2010.

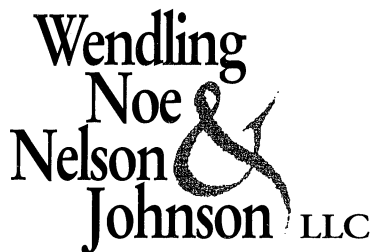
SOUTHWEST MEDICAL CENTER
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED
Years ended December 31, 2011 and 2010

Supplies and other expenses decreased by \$669,486 or 4.1 percent during 2011 and increased by \$60,670 or 0.4 percent during 2010. Of the total 2011 decrease, \$422,024 occurred due to discontinuing psychiatric inpatient services and \$257,515 was due to lower physician recruitment expenses. These changes are generally consistent with changes in patient volumes experienced by the Medical Center combined with the general rate of health care inflation.

The Foundation's operating results and changes in net assets for each of its last three years ended June 30 are summarized as follows:

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Contributions	\$165,420	\$ 22,954	\$ -
Investment income (loss)	772,267	478,298	(773,832)
Other income	119,465	117,935	83,845
Expenses	<u>(339,265)</u>	<u>(170,936)</u>	<u>(184,462)</u>
Increase (decrease) in net assets	<u>\$717,887</u>	<u>\$448,251</u>	<u>\$ (874,449)</u>

Unrealized gains and losses are included in the investment income category on the Foundation's financial statements. The Foundation's investment income included net realized and unrealized gains of \$616,822 during the year ended June 30, 2011, and \$347,042 during the year ended June 30, 2010, and net realized and unrealized losses of \$909,830 during the year ended June 30, 2009. These results followed changes in the broad market indices during those years.



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REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Trustees
Southwest Medical Center

We have audited the accompanying financial statements of the business-type activity and discretely presented component unit of Southwest Medical Center (the Medical Center) as of and for the years ended December 31, 2011 and 2010, which collectively comprise the Medical Center's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Medical Center's management. Our responsibility is to express opinions on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the Kansas Municipal Audit Guide. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Medical Center's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activity and discretely presented component unit of Southwest Medical Center as of December 31, 2011 and 2010, and their respective results of operations, changes in net assets, and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that management's discussion and analysis on pages 1 through 6 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our

inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Wendling Roe Nelson & Johnson LLC
Topeka, Kansas
March 26, 2012

FINANCIAL STATEMENTS

SOUTHWEST MEDICAL CENTER

BALANCE SHEETS

December 31,

ASSETS

	2011		2010	
	Medical Center	Component unit	Medical Center	Component unit
CURRENT ASSETS				
Cash and cash equivalents	\$ 1,707,283	\$ 653,667	\$ 1,418,895	\$ 667,957
Marketable securities		4,562,624		3,823,330
Assets limited as to use	1,631,649		792,055	
Patient accounts receivable, net of estimated uncollectibles of \$3,267,464 in 2011 and \$3,237,242 in 2010	5,819,462		5,918,109	
Estimated third-party payor settlements	10,445		201,034	
Other receivables	70,734		90,366	5,099
Inventories	1,322,661		1,246,458	
Prepaid expenses	1,280,934		1,177,654	
Total current assets	11,843,168	5,216,291	10,844,571	4,496,386
ASSETS LIMITED AS TO USE				
Internally designated	11,227,461		14,629,506	
Under indenture agreements - held by trustee	6,424,446		16,932,460	
By contributors and grantors for capital acquisitions	386,874		196,849	
	18,038,781	-	31,758,815	-
Less amounts required to meet current obligations	1,631,649		792,055	
Total assets limited as to use	16,407,132	-	30,966,760	-
CAPITAL ASSETS - NET	27,080,743	466,135	11,868,063	470,568
OTHER ASSETS				
Deferred financing costs, less accumulated amortization of \$29,516 in 2011 and \$11,207 in 2010	324,106		342,415	
Other investments		65,902		63,487
Total other assets	324,106	65,902	342,415	63,487
Total assets	\$55,655,149	\$ 5,748,328	\$54,021,809	\$ 5,030,441

The accompanying notes are an integral part of these statements.

LIABILITIES AND NET ASSETS

	2011		2010	
	Medical Center	Component unit	Medical Center	Component unit
CURRENT LIABILITIES				
Current maturities of long-term debt	\$ 175,000	\$ -	\$ 170,000	\$ -
Accounts payable	1,108,094		1,357,547	
Construction costs payable	1,215,538		415,748	
Estimated third-party payor settlements	521,353		277,485	
Other accrued liabilities	66,574		76,470	
Accrued salaries and benefits	822,207		586,297	
Accrued compensated absences	675,367		586,213	
Accrued interest payable	304,062		305,466	
Total current liabilities	4,888,195	-	3,775,226	-
LONG-TERM DEBT, less current maturities				
	16,910,941		17,111,698	
Total liabilities	21,799,136	-	20,886,924	-
NET ASSETS				
Invested in capital assets - net of related debt	13,118,890	466,135	8,911,129	470,568
Restricted				
For debt service	1,520,967		1,489,472	
Expendable for capital acquisitions	1,274,834		1,241,741	
For specific operating activities		340,462		229,859
Nonexpendable permanent endowments		508,703		507,887
Unrestricted	17,941,322	4,433,028	21,492,543	3,822,127
Total net assets	33,856,013	5,748,328	33,134,885	5,030,441
Total liabilities and net assets	\$55,655,149	\$ 5,748,328	\$54,021,809	\$ 5,030,441

SOUTHWEST MEDICAL CENTER
STATEMENTS OF REVENUES, EXPENSES,
AND CHANGES IN NET ASSETS
Year ended December 31,

	2011		2010	
	Medical Center	Component unit	Medical Center	Component unit
Operating revenues				
Net patient service revenue	\$39,128,105	\$ -	\$39,961,152	\$ -
Other	<u>672,900</u>		<u>630,292</u>	
Total operating revenues	<u>39,801,005</u>	<u>-</u>	<u>40,591,444</u>	<u>-</u>
Operating expenses				
Salaries and wages	16,772,571		16,730,778	
Employee benefits	4,359,652		4,640,131	
Supplies and other	15,821,663	334,832	16,491,149	166,503
Depreciation and amortization	<u>2,166,059</u>	<u>4,433</u>	<u>2,301,788</u>	<u>4,433</u>
Total operating expenses	<u>39,119,945</u>	<u>339,265</u>	<u>40,163,846</u>	<u>170,936</u>
Operating income (loss)	<u>681,060</u>	<u>(339,265)</u>	<u>427,598</u>	<u>(170,936)</u>
Nonoperating revenues (expenses)				
Investment income	169,078	772,267	239,274	478,298
Interest expense	(202,544)		(269,241)	
Noncapital grants and contributions	30,715	165,420	61,528	22,954
Loss on disposal of capital assets	(212,181)		(10,212)	
Loss on extinguishment of debt			(137,399)	
Other		<u>119,465</u>		<u>117,935</u>
Total nonoperating revenues (expenses)	<u>(214,932)</u>	<u>1,057,152</u>	<u>(116,050)</u>	<u>619,187</u>
Excess of revenues over expenses before capital grants and contributions	<u>466,128</u>	<u>717,887</u>	<u>311,548</u>	<u>448,251</u>
Capital grants and contributions	<u>255,000</u>		<u>80,000</u>	
Increase in net assets	<u>721,128</u>	<u>717,887</u>	<u>391,548</u>	<u>448,251</u>
Net assets at beginning of year	<u>33,134,885</u>	<u>5,030,441</u>	<u>32,743,337</u>	<u>4,582,190</u>
Net assets at end of year	<u>\$33,856,013</u>	<u>\$ 5,748,328</u>	<u>\$33,134,885</u>	<u>\$ 5,030,441</u>

The accompanying notes are an integral part of these statements.

SOUTHWEST MEDICAL CENTER
STATEMENTS OF CASH FLOWS
Year ended December 31,

	2011		2010	
	Medical Center	Component unit	Medical Center	Component unit
Cash flows from operating activities				
Receipts from and on behalf of patients	\$39,661,209	\$ -	\$39,203,915	\$ -
Payments to or on behalf of employees	(20,888,245)		(21,424,720)	
Payments for supplies and services	(16,179,409)	(334,832)	(16,290,759)	(166,503)
Other receipts and payments	692,532		731,369	
Net cash provided (used) by operating activities	3,286,087	(334,832)	2,219,805	(166,503)
Cash flows from noncapital financing activities				
Noncapital grants and contributions	30,715	165,420	61,528	22,954
Cash flows from capital and related financing activities				
Acquisition of capital assets	(16,369,917)		(2,486,674)	(26,688)
Issuance of long-term debt			18,167,463	
Principal payments on long-term debt	(170,000)		(1,795,000)	
Payment to extinguish debt			(3,123,571)	
Payment of deferred financing costs			(353,622)	
Interest paid	(739,550)		(293,503)	
Capital grants and contributions	255,000		80,000	
Proceeds from sale of equipment	33,583		1,251	
Insurance proceeds	72,069			
Net cash provided (used) by capital and related financing activities	(16,918,815)	-	10,196,344	(26,688)
Cash flows from investing activities				
Change in assets limited as to use	13,722,517		(12,539,872)	
Increase in investments		(122,472)		(98,600)
Other income received		160,543		129,617
Investment income received	167,884	117,051	252,162	202,169
Net cash provided (used) by investing activities	13,890,401	155,122	(12,287,710)	233,186
Net increase (decrease) in cash and cash equivalents	288,388	(14,290)	189,967	62,949
Cash and cash equivalents at beginning of year	1,418,895	667,957	1,228,928	605,008
Cash and cash equivalents at end of year	\$ 1,707,283	\$ 653,667	\$ 1,418,895	\$ 667,957

The accompanying notes are an integral part of these statements.

SOUTHWEST MEDICAL CENTER
STATEMENTS OF CASH FLOWS - CONTINUED
Year ended December 31,

	2011		2010	
	Medical Center	Component unit	Medical Center	Component unit
Reconciliation of operating income (loss) to net cash provided (used) by operating activities				
Operating income (loss)	\$ 681,060	\$ (339,265)	\$ 427,598	\$ (170,936)
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities				
Depreciation and amortization	2,166,059	4,433	2,301,788	4,433
Provision for bad debts	4,517,591		4,361,559	
Changes in				
Accounts receivable	(4,418,944)		(5,237,762)	
Other receivables	19,632		101,077	
Inventories and prepaid expenses	(179,483)		20,290	
Accounts payable and accrued expenses	65,715		126,289	
Estimated third-party payor settlements	434,457		118,966	
Net cash provided (used) by operating activities	<u>\$ 3,286,087</u>	<u>\$ (334,832)</u>	<u>\$ 2,219,805</u>	<u>\$ (166,503)</u>

The accompanying notes are an integral part of these statements.

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS
December 31, 2011 and 2010

NOTE A - DESCRIPTION OF REPORTING ENTITY AND SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES

1. Reporting entity

Southwest Medical Center (the Medical Center) is located in Liberal, Kansas, and is owned by Seward County, Kansas (the County), and governed by a seven-member Board of Trustees appointed by the Board of County Commissioners of the County. The Medical Center is a 101-bed, not-for-profit general hospital. The Medical Center can sue and be sued, and can buy, sell, or lease real property. Bond issuances must be approved by the County. The Medical Center is a component unit of the County.

The component unit discussed in Note A2 is included in the Medical Center's reporting entity because of the nature and significance of its relationship with the Medical Center.

2. Component unit

The financial statements include the financial data of the discretely presented component unit described below. The component unit is reported separately to emphasize that it is legally separate from the Medical Center.

Southwest Medical Center Foundation, Inc. (the Foundation), is a not-for-profit corporation formed in August of 1980 to receive, invest, and disburse funds received for the benefit, support, and maintenance of the Medical Center. The Foundation is administered by a Board of Trustees. Three of the seven members of that Board are also members of the Medical Center's Board of Trustees.

Financial data of the Foundation are presented as of June 30, 2011 and 2010, and for the years then ended.

3. Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

4. Basis of accounting

The Medical Center uses enterprise fund accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus. Pursuant to Governmental Accounting Standards Board (GASB) Statement No. 20, "Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting," the Medical Center has implemented all GASB pronouncements and only relevant pronouncements of the Financial Accounting Standards Board (FASB) issued before November 30, 1989.

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE A - DESCRIPTION OF REPORTING ENTITY AND SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES - Continued

5. Cash and cash equivalents

The Medical Center considers all cash and invested cash to be cash equivalents, excluding any assets limited as to use and items classified as investments by the Foundation.

6. Allowance for uncollectible accounts

The Medical Center provides for accounts receivable that could become uncollectible in the future by establishing an allowance to reduce the carrying value of such receivables to their estimated net realizable value. The Medical Center estimates this allowance based on the aging of its accounts receivable and its historical collection experience for each type of payor.

7. Inventories

Inventories are stated at the lower of cost or market with cost determined on the first-in, first-out method.

8. Investments and investment income

Investments in debt and equity securities are reported at fair value. Interest, dividends, and gains and losses, both realized and unrealized, on investments in debt and equity securities are included in nonoperating revenue when earned.

9. Assets limited as to use

Assets limited as to use include assets set aside by the Board of Trustees for replacement of capital assets or for purchase of additional capital assets, over which the Board retains control and may at its discretion subsequently use for other purposes; assets held by a trustee under indenture agreements; and assets restricted by contributors and grantors for capital acquisitions. Assets limited as to use that are required for obligations classified as current liabilities are reported in current assets.

10. Capital assets

Capital assets (including assets recorded as capital leases) are stated at cost. Depreciation and amortization of capital assets are provided on the straight-line method over the estimated useful lives of the assets. The estimated lives used are generally in accordance with the guidelines established by the American Hospital Association.

The costs of maintenance and repairs are charged to operating expenses as incurred. The costs of significant additions, renewals, and betterments to depreciable properties are capitalized and depreciated over the remaining or extended estimated useful lives of the item or the properties. Gains and losses on disposition of capital assets are included in nonoperating revenues and expenses.

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE A - DESCRIPTION OF REPORTING ENTITY AND SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES - Continued

11. Costs of borrowing

Interest costs (including amortization of deferred financing costs and bond premium) incurred on borrowed funds during the period of construction of capital assets are capitalized as a component of the cost of acquiring those assets. Costs incurred in connection with the issuance of long-term debt (including original issue premiums and discounts) are amortized using the interest method over the term of the related debt.

12. Grants and contributions

From time to time, the Medical Center receives grants and contributions from individuals and private organizations. Revenues from grants and contributions are recognized when all eligibility requirements, including time requirements, are met. Grants and contributions may be restricted for specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as nonoperating revenues. Amounts restricted to capital acquisitions are reported after nonoperating revenues and expenses.

13. Estimated health insurance claims payable

The Medical Center is self-insured for health insurance claims of its employees. Management estimates the net liability for reported and unreported claims incurred as of the end of each reporting period. These estimates are based on known claims and historical claims experience.

Management believes that estimates for health insurance claims payable are reasonable. However, it is possible that actual incurred claims expense may vary significantly from the estimate included in the accompanying financial statements.

14. Net assets

Net assets of the Medical Center are classified in four components. "Net assets invested in capital assets net of related debt" consist of capital assets net of accumulated depreciation and reduced by the balances of any outstanding borrowings used to finance the purchase or construction of those assets. "Restricted expendable net assets" are noncapital net assets that must be used for a particular purpose, as specified by creditors, grantors, or contributors external to the Medical Center, including amounts deposited with trustees as required by indenture agreements. "Restricted nonexpendable net assets" equal the principal portion of permanent endowments. "Unrestricted net assets" are remaining net assets that do not meet the definitions of the other three components of net assets.

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE A - DESCRIPTION OF REPORTING ENTITY AND SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES - Continued

15. Operating revenues and expenses

The Medical Center's statement of revenues, expenses, and changes in net assets distinguishes between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services, which is the Medical Center's principal activity. Nonexchange revenues, including noncapital grants and contributions, are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide health care services, other than financing costs.

16. Net patient service revenue

Net patient service revenue is reported at established charges with deductions for discounts, charity care, contractual adjustments, and provision for bad debts, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

17. Charity care

The Medical Center provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the Medical Center does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

18. Income taxes

The Medical Center is exempt from federal income taxes pursuant to Sections 115 and 501(a) of the Internal Revenue Code.

The Foundation is a not-for-profit corporation as described in Section 501(c)(3) of the Internal Revenue Code and is exempt from federal income taxes on its related income pursuant to Section 501(a) of the Code.

19. Subsequent events

The Medical Center has evaluated subsequent events through March 26, 2012, which is the date the financial statements were available to be issued.

NOTE B - REIMBURSEMENT PROGRAMS

The Medical Center has agreements with third-party payors that provide for payments to the Medical Center at amounts different from its established charge rates. The amounts reported on the balance sheets as estimated third-party payor settlements consist of the estimated differences between the

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE B - REIMBURSEMENT PROGRAMS - Continued

contractual amounts for providing covered services and the interim payments received for those services. A summary of the payment arrangements with major third-party payors follows:

Medicare - Inpatient acute care services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. Inpatient skilled nursing and psychiatric services are paid at prospectively determined per diem rates. Outpatient services are paid at prospectively determined rates per occasion of service. Physician services rendered to Medicare beneficiaries are paid based on a prospectively determined fee schedule. Prospectively determined rates vary according to patient classification systems that are based on clinical, diagnostic, and other factors. The Medical Center is paid for cost reimbursable and other items at tentative rates with final settlement determined after submission of annual cost reports by the Medical Center and audits or reviews thereof by the Medicare contractor. The Medical Center's classification of patients under the Medicare program and the appropriateness of their admission are subject to an independent review by a peer review organization. The Medical Center's Medicare cost reports have been audited or reviewed by the Medicare contractor through December 31, 2009.

Medicaid - Inpatient acute care services rendered to Medicaid program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. All other services rendered to Medicaid beneficiaries are paid at prospective rates determined on either a per diem or a fee-for-service basis.

Blue Cross and Blue Shield - All services rendered to patients who are insured by Blue Cross-Blue Shield are paid on the basis of prospectively determined rates per discharge or discounts from established charges.

The Medical Center has also entered into payment agreements with certain commercial insurance carriers and preferred provider organizations. The basis for payment to the Medical Center under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

A summary of gross and net patient service revenue follows:

	<u>2011</u>	<u>2010</u>
Gross patient service revenue	\$ 94,458,916	\$ 92,401,689
Contractual adjustments	(48,350,024)	(46,248,010)
Provision for bad debts	(4,517,591)	(4,361,559)
Charity care	<u>(2,463,196)</u>	<u>(1,830,968)</u>
Net patient service revenue	<u>\$ 39,128,105</u>	<u>\$ 39,961,152</u>

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE B - REIMBURSEMENT PROGRAMS - Continued

Revenue from the Medicare and Medicaid programs accounted for approximately 23 percent and 11 percent, respectively, of the Medical Center's net patient service revenue during 2011, and 25 percent and 12 percent, respectively, of the Medical Center's net patient service revenue during 2010. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

NOTE C - DEPOSITS WITH FINANCIAL INSTITUTIONS

Kansas statutes authorize the Medical Center, with certain restrictions, to deposit or invest in open accounts, time deposits, certificates of deposit, repurchase agreements, U.S. Treasury Bills and Notes, and the State Treasurer's investment pool. Kansas statutes also require that collateral be pledged for bank deposits with a fair market value equal to 100 percent of the uninsured amounts and must be assigned for the benefit of the Medical Center.

At December 31, 2011, the carrying amount of the Medical Center's bank deposits, including certificates of deposit, was \$13,308,341 and the bank balances were \$14,819,773. Of the bank balances, \$500,000 was covered by federal depository insurance and \$14,319,773 was covered by collateral held by a third-party bank, but not registered in the Medical Center's name.

The Medical Center's bank deposits are included in the financial statements under the following categories:

Cash and cash equivalents	\$ 1,703,859
Assets limited as to use	
Internally designated	11,217,608
By contributors and grantors	
for capital acquisitions	<u>386,874</u>
Total bank deposits	<u>\$ 13,308,341</u>

NOTE D - INVESTMENTS

The Foundation's investments are stated at fair value. The composition of its investments is as follows:

	<u>2011</u>	<u>2010</u>
Equity securities	\$ 4,127,920	\$ 3,499,994
Fixed income securities	<u>434,704</u>	<u>323,336</u>
	<u>\$ 4,562,624</u>	<u>\$ 3,823,330</u>

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE E - ASSETS LIMITED AS TO USE

The composition of assets limited as to use is as follows:

	<u>2011</u>	<u>2010</u>
Internally designated		
Cash	\$ 1,217,608	\$ 2,122,136
Certificates of deposit	10,000,000	12,500,000
Accrued interest receivable	<u>9,853</u>	<u>7,370</u>
	<u>\$ 11,227,461</u>	<u>\$ 14,629,506</u>
Under indenture agreements - held by trustee		
U.S. Treasury obligations	\$ 5,415,545	\$ 15,923,559
State and local government obligations	992,501	992,501
Accrued interest receivable	<u>16,400</u>	<u>16,400</u>
	<u>\$ 6,424,446</u>	<u>\$ 16,932,460</u>
By contributors and grantors for capital acquisitions		
Cash	<u>\$ 386,874</u>	<u>\$ 196,849</u>

NOTE F - CAPITAL ASSETS

Capital asset additions, retirements, and balances for the Medical Center are as follows:

	<u>2011</u>			
	<u>Beginning balance</u>	<u>Transfers and additions</u>	<u>Retirements</u>	<u>Ending balance</u>
Land	\$ 43,012	\$ -	\$ -	\$ 43,012
Land improvements	903,176			903,176
Buildings and fixed equipment	23,992,860	174,428		24,167,288
Major movable equipment	<u>28,809,112</u>	<u>1,958,601</u>	<u>62,952</u>	<u>30,704,761</u>
Totals at historical cost	<u>53,748,160</u>	<u>2,133,029</u>	<u>62,952</u>	<u>55,818,237</u>
Less accumulated depreciation and amortization				
Land improvements	816,617	12,865		829,482
Buildings and fixed equipment	19,614,475	648,358		20,262,833
Major movable equipment	<u>24,010,424</u>	<u>1,504,836</u>	<u>29,369</u>	<u>25,485,891</u>
	<u>44,441,516</u>	<u>2,166,059</u>	<u>29,369</u>	<u>46,578,206</u>
	9,306,644	(33,030)	33,583	9,240,031
Construction in progress	<u>2,561,419</u>	<u>15,563,543</u>	<u>284,250</u>	<u>17,840,712</u>
Capital assets, net	<u>\$ 11,868,063</u>	<u>\$ 15,530,513</u>	<u>\$ 317,833</u>	<u>\$ 27,080,743</u>

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE F - CAPITAL ASSETS - Continued

	2010			
	<u>Beginning balance</u>	<u>Transfers and additions</u>	<u>Retirements</u>	<u>Ending balance</u>
Land	\$ 43,012	\$ -	\$ -	\$ 43,012
Land improvements	903,176			903,176
Buildings and fixed equipment	23,786,592	206,268		23,992,860
Major movable equipment	27,839,851	992,186	22,925	28,809,112
Totals at historical cost	<u>52,572,631</u>	<u>1,198,454</u>	<u>22,925</u>	<u>53,748,160</u>
Less accumulated depreciation and amortization				
Land improvements	803,322	13,295		816,617
Buildings and fixed equipment	18,666,688	947,787		19,614,475
Major movable equipment	<u>22,681,180</u>	<u>1,340,706</u>	<u>11,462</u>	<u>24,010,424</u>
	<u>42,151,190</u>	<u>2,301,788</u>	<u>11,462</u>	<u>44,441,516</u>
	10,421,441	(1,103,334)	11,463	9,306,644
Construction in progress	<u>545,214</u>	<u>2,016,205</u>		<u>2,561,419</u>
Capital assets, net	<u>\$10,966,655</u>	<u>\$ 912,871</u>	<u>\$ 11,463</u>	<u>\$11,868,063</u>

Construction in progress consists primarily of costs incurred to date for renovations and additions to the Medical Center's facilities. A summary of outstanding contract commitments for the construction project at December 31, 2011, is as follows:

Total commitment	\$ 15,872,096
Costs incurred to date	<u>(12,502,796)</u>
Remaining commitment	<u>\$ 3,369,300</u>

Capital asset additions, retirements, and balances for the Foundation are as follows:

	2011			
	<u>Beginning balance</u>	<u>Transfers and additions</u>	<u>Retirements</u>	<u>Ending balance</u>
Land	\$ 435,560	\$ -	\$ -	\$ 435,560
Land improvements	96,231			96,231
Major movable equipment	<u>2,079</u>			<u>2,079</u>
Totals at historical cost	533,870	-	-	533,870
Less accumulated depreciation and amortization	<u>63,302</u>	<u>4,433</u>		<u>67,735</u>
Capital assets, net	<u>\$ 470,568</u>	<u>\$ (4,433)</u>	<u>\$ -</u>	<u>\$ 466,135</u>

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE F - CAPITAL ASSETS - Continued

	2010			
	<u>Beginning balance</u>	<u>Transfers and additions</u>	<u>Retirements</u>	<u>Ending balance</u>
Land	\$ 435,560	\$ -	\$ -	\$ 435,560
Land improvements	69,543	26,688		96,231
Major movable equipment	<u>2,079</u>			<u>2,079</u>
Totals at historical cost	507,182	26,688	-	533,870
Less accumulated depreciation and amortization	<u>58,869</u>	<u>4,433</u>		<u>63,302</u>
Capital assets, net	<u>\$ 448,313</u>	<u>\$ 22,255</u>	<u>\$ -</u>	<u>\$ 470,568</u>

NOTE G - LONG-TERM DEBT

Long-term debt consists of the following:

	<u>2011</u>	<u>2010</u>
2.0% to 5.0% General Obligation Hospital Refunding and Improvement Bonds, Series 2010-A; issued on May 27, 2010, in the original amount of \$17,670,000, due serially through August 1, 2040	\$ 16,630,000	\$ 16,800,000
Net unamortized premium (discount)	<u>455,941</u>	<u>481,698</u>
	17,085,941	17,281,698
Less current portion	<u>175,000</u>	<u>170,000</u>
	<u>\$ 16,910,941</u>	<u>\$ 17,111,698</u>

On May 27, 2010, the County issued \$17,670,000 in General Obligation Hospital Refunding and Improvement Bonds, Series 2010-A, (the 2010-A bonds) on behalf of the Medical Center pursuant to a bond trust indenture dated May 1, 2010. The proceeds of the bonds were used, together with other available funds of the Medical Center, for the purpose of providing funds to (1) expand and renovate the Medical Center's existing facilities, (2) pay for the costs of certain items of equipment, (3) fund a debt service reserve fund, (4) pay certain costs related to issuance of the bonds, and (5) make the payment as scheduled on August 1, 2010, for principal and interest due then on the 2001-A bonds.

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE G - LONG-TERM DEBT - Continued

On November 1, 2010, the County engaged in a current refunding of the 2001-A bonds then outstanding by making an irrevocable deposit with a trustee of \$3,119,280 of available funds of the Medical Center. Those funds were used by the trustee to purchase direct obligations of the United States of America that would mature and pay interest in amounts and at times that provided for payment of principal and interest on the 2001-A bonds through August 1, 2011, and to redeem and pay the 2001-A bonds remaining outstanding on that date at a redemption price of 100 percent. A loss on extinguishment of debt of \$137,399 was recognized in the 2010 financial statements because the acquisition cost of the extinguished debt was greater than the net carrying amount of that debt on the balance sheet.

The indenture agreements for the bonds require the Medical Center to transfer to a trustee, on a monthly basis, specified amounts which, when combined with interest earned on the respective funds held by the trustee, will provide sufficient funds to pay the bond principal and interest on the appropriate due dates. Such amounts were maintained and are included with assets limited as to use in the financial statements. The indenture agreements also include certain restrictive covenants relating to the acquisition and disposition of property, incurrence of additional indebtedness, and level of fees and rates charged.

Scheduled annual debt service requirements on long-term debt are as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2012	\$ 175,000	\$ 736,150	\$ 911,150
2013	180,000	732,650	912,650
2014	355,000	729,050	1,084,050
2015	360,000	721,063	1,081,063
2016	370,000	712,063	1,082,063
2017 - 2021	2,040,000	3,373,500	5,413,500
2022 - 2026	2,420,000	2,991,565	5,411,565
2027 - 2031	3,025,000	2,395,000	5,420,000
2032 - 2036	3,865,000	1,558,500	5,423,500
2037 - 2040	3,840,000	491,750	4,331,750
	<u>\$ 16,630,000</u>	<u>\$ 14,441,291</u>	<u>\$ 31,071,291</u>

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE G - LONG-TERM DEBT - Continued

The following is a summary of changes in long-term debt:

Principal outstanding at January 1, 2010	\$ 3,925,000
Issuance of long-term debt	17,670,000
Payment to extinguish debt	(3,000,000)
Principal payments	<u>(1,795,000)</u>
Principal outstanding at January 1, 2011	16,800,000
Principal payments	<u>(170,000)</u>
Principal outstanding at December 31, 2011	<u>\$ 16,630,000</u>

Total interest costs are summarized as follows:

	<u>2011</u>	<u>2010</u>
Total interest incurred	\$ 738,146	\$ 563,016
Amortization of deferred financing costs, and bond premium and discount	<u>(7,448)</u>	<u>19,423</u>
	730,698	582,439
Less interest earned on borrowed funds offset against capitalized interest costs	(1,284)	(961)
Net capitalized interest costs	<u>(526,870)</u>	<u>(312,237)</u>
Interest expense	<u>\$ 202,544</u>	<u>\$ 269,241</u>

NOTE H - DEFINED BENEFIT PENSION PLAN

The Medical Center participates in the Kansas Public Employees Retirement System (KPERS), a cost-sharing multiple-employer defined benefit pension plan as provided by K.S.A. 74-4901, et. seq. Substantially all employees of the Medical Center are eligible to participate in KPERS following the completion of one year of service. KPERS provides retirement benefits, life insurance, disability income benefits, and death benefits. Kansas law establishes and amends benefit provisions. KPERS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to KPERS (611 S. Kansas Avenue, Topeka, Kansas 66603-3803) or by calling 1-888-275-5737.

K.S.A. 74-4919 establishes the KPERS member-employee contribution rate at 4 percent of covered salary for employees hired prior to July 1, 2009, and 6 percent of covered salary for employees hired on or after July 1, 2009. The employer collects and remits member-employee contributions according to the provisions of Section 414(h) of the Internal Revenue Code. State law provides that the employer contribution rate be determined annually based on the results of an annual actuarial valuation.

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE H - DEFINED BENEFIT PENSION PLAN - Continued

KPERS is funded on an actuarial reserve basis. State law sets a limitation on annual increases in the contribution rates for KPERS employers. The employer rates established by statute for calendar years 2011 and 2010 were 7.49 percent and 6.89 percent, respectively. The Medical Center's employer contributions to KPERS for the years ended December 31, 2011 and 2010, were \$1,175,435 and \$1,095,972, respectively, equal to the statutory required contributions for each year.

NOTE I - EMPLOYEE HEALTH INSURANCE

The Medical Center is self-insured for health insurance claims of its employees. The Medical Center has reinsured a portion of its risk for such claims. The reinsurance arrangement covers annual claims in excess of \$75,000 for each covered individual. The reinsurance arrangement also covers aggregate annual claims in excess of an amount determined in relation to the number of individuals participating in the self-insured health benefits plan during the year. Covered employees also provide part of the funds to pay claims through monthly contributions at predetermined rates. Contributions by the Medical Center and participating employees are remitted to the Southwest Medical Center Employee Health Plan Trust. The Trust has retained an insurance company as its agent to process and settle claims. The Trust reimburses the agent weekly for the amount of claims paid by the agent net of any amounts covered by reinsurance. The following is a summary of the activity under this arrangement:

	<u>2011</u>	<u>2010</u>
Estimated net health insurance claims payable at beginning of year	\$ 315,082	\$ 390,120
Provision for Medical Center's share of incurred claims and related expenses for the year, net of any reinsurance proceeds	1,663,964	1,751,582
Employee contributions	677,304	691,440
Payments made for claims and related expenses	<u>(2,418,709)</u>	<u>(2,518,060)</u>
Estimated net health insurance claims payable at end of year	237,641	315,082
Trust assets available for payment of claims and related expenses	<u>1,053,583</u>	<u>1,049,732</u>
Net estimated prepaid expense for health insurance claims at end of year	<u>\$ (815,942)</u>	<u>\$ (734,650)</u>

SOUTHWEST MEDICAL CENTER
NOTES TO FINANCIAL STATEMENTS - CONTINUED
December 31, 2011 and 2010

NOTE J - CONCENTRATION OF CREDIT RISK

The Medical Center grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors at December 31, 2011 and 2010, is as follows:

	<u>2011</u>	<u>2010</u>
Medicare	25%	23%
Medicaid	13	15
Blue Cross	9	11
Other third-party payors	24	25
Self-pay	<u>29</u>	<u>26</u>
	<u>100%</u>	<u>100%</u>

NOTE K - RELATED PARTY TRANSACTIONS

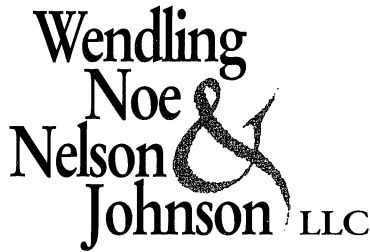
During 2011 and 2010, the Medical Center received \$255,000 and \$80,000, respectively, from the Foundation for the purchase of property and equipment.

NOTE L - RISK MANAGEMENT

For the years ended December 31, 2011 and 2010, the Medical Center was insured for professional liability under a comprehensive hospital liability policy provided by an independent insurance carrier with limits of \$200,000 per occurrence up to an annual aggregate of \$600,000 for all claims made during the policy year. The Medical Center is further covered by the Kansas Health Care Stabilization Fund for claims in excess of its comprehensive hospital liability policy up to \$800,000 pursuant to any one judgment or settlement against the Medical Center for any one party, subject to an aggregate limitation for all judgments or settlements arising from all claims made in the policy year in the amount of \$2,400,000. The policy provided by the independent insurance carrier provides for umbrella liability coverage in excess of the underlying limits set forth above in the amount of \$2,000,000 per occurrence with an aggregate amount in any policy year of \$2,000,000. All coverage is on a claims-made basis. The above policies are currently in effect through November 21, 2012. The Medical Center intends to renew this coverage on that date and is aware of no reason why such coverage would be denied at that time.

In addition to the risks disclosed elsewhere in these financial statements and notes thereto, the Medical Center is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Medical Center purchases commercial insurance for these risks. Settled claims have not exceeded this commercial coverage in any of the past three years.

SUPPLEMENTAL INFORMATION



Certified Public Accountants
and Management Consultants

Brian J. Florea, CPA
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REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS
ON SUPPLEMENTAL INFORMATION

Board of Trustees
Southwest Medical Center

We have audited the financial statements of Southwest Medical Center as of and for the years ended December 31, 2011 and 2010, and have issued our report thereon dated March 26, 2012, which contained an unqualified opinion on those financial statements. Our audit was performed for the purpose of forming an opinion on the financial statements as a whole. The supplemental information presented hereinafter is presented for the purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole, except that no opinion is expressed as to the adequacy of insurance coverage.

Wendling Noe Nelson & Johnson LLC
Topeka, Kansas
March 26, 2012

SOUTHWEST MEDICAL CENTER
BALANCE IN DEPOSITORY COMPARED WITH DEPOSITORY SECURITY
December 31, 2011

	<u>Bank balances</u>	<u>F.D.I.C. coverage</u>	<u>Balance subject to pledging of securities</u>	<u>Market value of securities pledged</u>	<u>Market value of securities pledged in excess of (less than) depository requirements</u>
First National Bank	\$ 7,319,773	\$ 250,000	\$ 7,069,773	\$ 7,875,500	\$ 805,727
Community Bank	7,500,000	250,000	7,250,000	8,185,079	935,079

SOUTHWEST MEDICAL CENTER
SCHEDULE OF REVENUES AND EXPENSES
WITH BUDGET COMPARISON
Year ended December 31, 2011

	<u>Actual</u>	<u>Budget</u>	<u>Over (under)</u>
Net patient service revenue	\$ 39,128,105	\$ 40,391,000	\$ (1,262,895)
Other	<u>672,900</u>	<u>656,000</u>	<u>16,900</u>
Total operating revenues	39,801,005	41,047,000	(1,245,995)
Total operating expenses	<u>39,119,945</u>	<u>40,425,000</u>	<u>(1,305,055)</u>
Operating income	681,060	622,000	59,060
Nonoperating revenues (expenses)	<u>(214,932)</u>	<u>(248,000)</u>	<u>33,068</u>
Excess of revenues over expenses before capital grants and contributions	<u>\$ 466,128</u>	<u>\$ 374,000</u>	<u>\$ 92,128</u>

SOUTHWEST MEDICAL CENTER
SUMMARY OF INSURANCE COVERAGE

December 31, 2011

<u>Insurer</u>	<u>Type of coverage</u>	<u>Coverage amount</u>	<u>Term</u>
KaMMCO Insurance Company	Hospital professional liability Other liability Personal injury/property	HPL \$200,000/\$600,000 PL \$1,000,000/\$3,000,000 PIP \$1,000,000/\$1,000,000	November 21, 2011 to November 21, 2012
Kansas Health Care Provider Insurance Availability Act	Excess hospital professional liability	\$800,000/\$2,400,000	November 21, 2011 to November 21, 2012
KaMMCO Insurance Company	Umbrella liability	\$2,000,000/\$2,000,000	November 21, 2011 to November 21, 2012
Darwin Insurance Co.	Directors, Officers, and Trustees liability	\$2,000,000/\$2,000,000	November 21, 2011 to November 21, 2012
KaMMCO Insurance Company	Limited pollution liability	\$50,000/\$50,000	November 21, 2011 to November 21, 2012
Travelers Insurance Company	Property	Real - \$35,938,038 Personal - \$25,410,011 Business interruption - \$38,601,250	June 30, 2011 to June 30, 2012
Travelers Insurance Company	Auto liability and physical damage	\$1,000,000/\$1,000,000	June 30, 2011 to June 30, 2012
Travelers Insurance Company	Commercial crime	Blanket employee dishonesty and forgery/alteration - \$100,000 Excess employee dishonesty- \$250,000 Theft, burglary - \$10,000	June 30, 2011 to June 30, 2012
KHA Workers' Compensation Fund, Inc.	Workers' compensation and employers liability (Kansas)	Statutory: Bodily injury by accident - \$500,000 each accident Bodily injury by disease - \$500,000 policy limit Bodily injury by disease - \$500,000 each employee	January 1, 2011 to January 1, 2012